Supreme Court of the United States

OCTOBER TERM, 1958

No. 174

UNITED STATES OF AMERICA,
Petitioner,

vs.

EMBASSY RESTAURANT, INC., et al.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF OF NATIONAL ASSOCIATION OF CREDIT MANAGEMENT, INC., AS *AMICUS CURIAE*

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Interest of the Amicus Curiae

The amicus curiae, National Association of Credit Management, Inc. (formerly known as National Association of Credit Men), hereinafter referred to as the "Association", is a non-profit membership corporation consisting of approximately 35,000 manufacturers, bankers and jobbers throughout the United States all of whom are engaged in businesses involving the extension of unsecured credit to their customers.

The Association was organized in 1896 for the express purpose amongst others of urging the enactment

by Congress of a national bankruptcy act. Since the accomplishment of this purpose, one of its primary aims has been the improvement of bankruptcy law and procedure. The Association contributes financially to the support of the National Bankruptcy Conference, and its counsel has at all times taken an active part in the work of the Conference."

The Association's interest in the case at bar arises from the fact that the claims of its members in bankruptcy proceedings are usually unsecured general claims, which share last in the distribution of the assets, and any interpretation of the Bankruptcy Act which extends the class of persons entitled to priority necessarily diminishes the meager funds available for the payment of non-priority claims.

Statute Involved

Section 64 a of the Bankruptcy Act (11 U. S. C. Sec. 104 a), so far as here relevant, provides as follows:

> "a. The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be * * * (2) wages, not to exceed $600 to each claimant, which have been earned within three months before the date of the commencement of the proceeding, due to workmen, servants, clerks, or travelling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt; * * * (4) taxes legally due and owing by the bankrupt to the United States or any state or any subdivision thereof * * *."

Question Presented

Are payments due by an employer to the trustees of a union welfare fund pursuant to a collective bargaining agreement "wages * * * due to workmen" within the purview of Section 64 a (2) of the Bankruptcy Act, where there is no assignment of any part of their wages by the employees to the trustees of the fund, and where the trust agreement provides: (a) that the employer's contributions to the fund shall not constitute or be deemed moneys due the individual employees; (b) that said moneys shall not be liable for or subject to the debts, contracts, liabilities, or torts of the parties entitled to such money upon the termination of the plan; and (c) the trust fund is to be administered not only for the benefit of employees of the employer included in the collective bargaining unit, but also for the benefit of employees of the union.

Facts

We assume that the facts will be fully presented by the parties to this appeal, and we shall not repeat them except as necessary to the argument.

POINT I

Allowance of the claims of the trustees as priority "wage" claims does violence to the rule that rights of priority granted by the Bankruptcy Act should be strictly construed.

The lower courts are unanimous in holding that the priorities fixed by Section 64 of the Bankruptcy Act must be adhered to, and may not be varied or departed from, *In re Columbia Ribbon Co.*, 117 F. (2d) 999 (C. A. 3, 1941); claimants seeking priority must clearly establish their rights thereto, *In re Public Ledger*, 63 Fed. Supp. 1008, 1016 (1945); and such statutes must be strictly construed, *In re Wilt Dairy Co.*, 48 Fed. Supp. 964, 968 (1942); *In re Penticoff*, 36 Fed. Supp. 1 (1941); *In re Paradise Catering Corp.*, 36 Fed. Supp. 974 (1941); 3 *Collier on Bankruptcy* (14th Ed.) p. 2058.

The limited priority granted to wage claims by Section 64 of the Act was designed to protect those who are dependent upon their current earnings for their daily needs, and who, because of the employer's bankruptcy, might otherwise be in dire need of funds to satisfy the immediate requirements of themselves and their families. *Blessing* vs. *Blanchard*, 223 Fed. 35 (1915); and to reward and protect those who created assets for the bankrupt estate shortly before bankruptcy intervened. *In re Raiken*, 33 Fed. Supp. 88 (1940).

In *Matter of Brassel*, 135 Fed. Supp. 827 (1955), the court had before it a claim similar to that advanced in the instant case. In an exceptionally well-

reasoned opinion, which is based upon facts substantially the same as in the instant case, the court denied the claim of the trustees of the welfare fund to priority for the bankrupt employer's contributions to the fund. Holding that the term "wages" as used in Section 64 a (2) of the Bankruptcy Act does not include such contributions, the court said, at page 830:

> "If contributions to a fund by an employer are to be construed as 'wages' and as covered by the provisions of Section 64, sub. a (2) of the Act, its purpose of protection would be greatly weakened by present day conditions. A contribution of even a small percentage of the gross weekly payroll of a great number of employers would exceed the amount of $600 even in a single week.
>
> "The ultimate contention here however is one of priority. Liberality of construction of the term 'wages' does not justify a nullification of the language of the statute which grants priority only to 'wages * * * due to workmen'. The employers' contribution here is never due to the employee. He may not enforce the employers' liability therefor. The employee never had an individual or assignable proprietory interest in the contribution or to the fund of which the contribution became a part. The discretion of the trustees in the administration of the fund is final and conclusive. The contributions here may be entirely exhausted by the expense of administration or by benefits allotted to union members possessing union seniority who never have been employed by a contributing employer. Here there is no claim of an assignment by the employees. It was not the intention of the section to afford priority pro-

tection to entire strangers. The claim is not entitled to priority."

Commenting upon this decision, the *Chicago Kent Law Review* said (Vol. XXXIV, at page 238):

> "Even under the most liberal construction of all the terms of the relevant portions of the statute, the claimant was not a workman or an assignee of a workman; the sum claimed did not represent wages in the ordinary sense of the term, and the amount payable, while measured by the amount of wages earned, formed no more than a contractual obligation owed to a third person. No degree of liberality in connection with the construction of the terms of the statute could justify the amount of nullification in the language of the Act, much less justify the overruling of the long standing and incontrovertible decisions holding otherwise, which would be necessary before a claim of the kind asserted could be upheld. If the fringe benefits now common under modern mass employment contracts are to be protected against the impact of bankruptcy, substantial revision would have to be made both in the statutory language and in the fundamental principles concerning priorities."

As in the *Brassel* case, the employer's contributions to the welfare fund in the case here under review, while measured by the amount of wages paid to the employees, were not to be deducted from wages; were not assigned by the wage earners to the trustees; were not held in trust by the employer for the benefit of the wage earners; were never payable to the wage earners; were not subject to federal withholding or

income taxation; and were not considered wages under the Insurance Contributions Act (Social Security Law, 26 U. S. C. Sec. 3121 (a) (2)).

The Declaration of Trust (R. p. 22), provides:

> "The monies to be paid into the said Local 111, Welfare Plan shall not constitute or be deemed monies due to the individual employees, nor shall said monies in any manner be liable for or subject to the debts, contracts, liabilities or torts of the parties entitled to such money upon the termination of the Local 111, Welfare Fund."

In *Local 140 Security Fund* vs. *Hack*, 242 F. (2d) 375 (1957), the Court of Appeals for the Second Circuit had before it a similar claim. Holding that the employer's agreed contributions to the union welfare fund did not constitute wages within the meaning of the Act, the court said, at pp. 377, 378:

> "The claim in its origin must be one for wages due to a workman entitled to priority under Section 64, sub. a (2). If it is, the right of priority carried over to the workman's assignee. If the claim was never a part of his wages and was never a sum due to him, it would not be entitled to priority; and no theory of an indirect conditional benefit to him can give it priority. 'The priority is attached to the debt and not to the person of the creditor; to the claim and not to the claimant.'
>
> * * * *
>
> "What were specified in the collective bargaining agreement * * * as payments by the employer to Local 140 Security Fund * * * created only a

debtor and creditor obligation between the employer and third parties, for something other than wages. The language of the statute granting priority to wages cannot be stretched so as to embrace this type of claim. If every type of payment made by an employer to a union welfare fund is to be given priority as a claim for 'wages' * * * that should be done through the legislative action of the Congress, and not by any judicial mislabelling of such payments as 'wages'."

In the opinion in the instant case, the court below cited, in support of its decision, the decision of this court in *U. S.* vs. *Carter,* 353 U. S. 210. There the question was whether the trustees of a union welfare fund could maintain an action against the surety on a bond given by a contractor pursuant to the requirements of the Miller Act (40 U. S. C. Secs. 270 et seq.), which provides that Government contractors shall furnish a payment bond for the protection of "all persons supplying labor and material in the prosecution of the work."

This court held that the Miller Act is highly remedial and should be liberally construed to effectuate its protective purposes, and that the surety's liability on a bond issued under the statute must be at least coextensive with the obligations imposed by the Act if the bond is to have its intended effect. The court pointed out, however, that *"the Act * * * does not limit recovery on the statutory bond to 'wages'."* (p. 217). (Emphasis supplied.)

To effectuate the remedial purposes of the *Miller Act*, a liberal construction is necessary; but the reme-

dial purposes of the wage priority granted by the Bankruptcy Act are best served by a construction which does not extend the meaning of the word "wages" and which confines the limited right of priority to claims for wages in the usually accepted sense of the term.

The fact that the wage priority created by Section 64 a (2) limits the priority to each individual claimant to $600, makes it impractical to include claims such as those here at issue, for if such claims are classified as wages and granted priority, they will rank on a parity with the personal claims of individual wage earners, and the right of the individual wage earners to their $600 may be seriously impaired. It is difficult to believe that Congress ever contemplated such a situation.

Thus, if there were due to an employee $600 of wages, earned within three months before the date of bankruptcy, and the employer were in default in his payments to be made to the union welfare fund and measured by such employee's services, to the extent of $600 due within three months before bankruptcy, the $600 statutory priority would have to be apportioned between the employee and the trustees, thereby depriving the employee of all or part of the monies which he would otherwise have been entitled to receive.

If priority is to be granted to an employer's contributions to a union welfare fund, Congress, after a public hearing at which unsecured creditors, wage earners, the taxing authorities, and other affected parties would have an opportunity to be heard, should amend the Act to create a separate priority classification.

POINT II

The policy of Congress as expressed in recent legislation has been to limit priorities in order to protect the interests of general creditors.

Until the enactment of the Chandler Act on June 2, 1938, there was a tendency for the typical bankruptcy proceeding to resolve itself into a process in which one preferred party after another sliced off a portion of the available assets, with little or nothing remaining for distribution to general creditors. *In re Standard Composition Co.*, 23 Fed. Supp. 391, 395 (1938); *In re Pacific Oil and Meal Co.*, 24 Fed. Supp. 767, 771 (1938). Priorities created by state laws were recognized on a parity with priorities created by the laws of the United States, and the priority which might be allowed to a landlord's claim for rent was unlimited.

The Chandler Act repealed the provision recognizing state priorities, and limited the claims of landlords to rent legally due and owing on the date of bankruptcy and which accrued within three months prior thereto.

Currently, Congress is considering the enactment of a bill to reduce the priority of tax claims (now unlimited; Act Sec. 64 a (4)) to taxes which became legally due and owing within three years prior to the date of bankruptcy. Such a bill, drafted and supported by the National Bankruptcy Conference, passed the House of Representatives at the last session of Congress (H. R. 12802), and is expected to be reintroduced at the next session of Congress.

Shortly after the decision of the Court of Appeals for the Second Circuit in *Local 140 Security Fund* vs. *Hack, supra,* the Chairman of the Judiciary Committee of the House of Representatives introduced in the First Session of the 85th Congress a bill, known as H. R. 8805, which, in effect, would have reversed the holding of the *Hack* case. The bill was not enacted, and has not since been re-introduced. We may assume that Congress was satisfied with the legal status of this question as resolved by the *Hack* decision.

This court has held that "the theme of the Bankruptcy Act is 'equality of distribution', *Sampsell* vs. *Imperial Paper and Color Corp.,* 313 U. S. 215, 219; and if one claimant is to be preferred over others, the purpose should be clear from the statute." *Nathanson* vs. *Nat'l. Labor Relations Board,* 344 U. S. 26, 28-29 (1952).

Where, as here, a strained construction of the statute is necessary to sustain a claim of priority, it seems obvious that there cannot have been a clear intent to create the priority.

No social reason appears why the claim of the trustees of a welfare fund should be accorded a priority status as against the claims of unsecured creditors who have extended to the bankrupt the credit which enabled him to operate and pay wages, *especially where, as here, the fund is for the benefit of employees of the union, as well as employees of the bankrupt employer.* (Record p. 10; Agreement & Declaration of Trust, Article I, Section 3).

CONCLUSION

For the reasons above stated, we believe that the decision of the court below should be reversed.

Dated, New York, New York, November 28, 1958.

Respectfully submitted,

W. RANDOLPH MONTGOMERY,
Attorney for National Association of Credit Management, Inc., as amicus curiae